

1
2
3
4
5
6 UNITED STATES DISTRICT COURT
7 WESTERN DISTRICT OF WASHINGTON
8 AT SEATTLE

9 JASON MOOMJY,

10 Plaintiff,

11 v.

12 HQ SUSTAINABLE MARITIME
13 INDUSTRIES, INC., *et al.*,

14 Defendants.

Case No. C11-0726RSL

ORDER GRANTING
MOTIONS TO STAY
STATE COURT DISCOVERY

15
16 **I. INTRODUCTION**

17 This matter comes before the Court on two motions – one filed by HQ Sustainable
18 Maritime Industries, Inc. and one filed by the individual defendants – for a stay of
19 discovery in a pending state court derivative action. The action in this Court was
20 brought on behalf of all persons who purchased or otherwise acquired HQ’s common
21 stock between May 11, 2009 and April 1, 2011 (the “Class Period”), pursuant to
22 §§ 10(b) and 20(a) of the Securities Exchange Act of 1934 and Securities and Exchange
23
24
25

Commission Rule 10b-5.¹

II. DISCUSSION

A. Background Facts.

This securities class action was filed on April 28, 2011. Shortly thereafter, six different groups of plaintiffs filed complaints asserting claims derivatively on behalf of the company against various directors and officers, two of whom are defendants in this action. Four of those cases have been consolidated before this Court. Hopkins v. HQ Sustainable Maritime Industries, Inc., C11-910RSL. The other two actions were filed in King County Superior Court and consolidated under the caption In re HQ Sustainable Maritime Indus., Inc. Derivative Litig., Civ. No. 11-2-16742-9-SEA (the “state court action”).

In June 2011, the plaintiffs in the state court action (“plaintiffs”) served their first requests for production. Approximately two weeks later, they served their first set of interrogatories. Both sets were served on the company and the individual defendants. Defendants moved for a stay of the state court discovery. On August 8, 2011, King County Superior Court Judge Kim Prochnau issued an order holding that the “court does not find good cause to stay discovery pending federal action or motions to dismiss this action,” but “finds good cause to appoint a discovery master given complexity of action, multiplicity of actions and likely issues regarding discovery.” Notice of Recent Ruling, (Dkt. #76), Ex. A. Only the state court plaintiffs have responded to and opposed defendants’ motion for a discovery stay before this Court.

¹ Because this matter can be decided based on the parties’ filings and the balance of the record, their request for oral argument is denied.

1 **B. Analysis.**

2 The Private Securities Litigation Reform Act (“PSLRA”) imposes a discovery
3 stay in private federal securities litigation while a motion to dismiss is pending. 15
4 U.S.C. § 78u-4(b)(3)(B). In 1998, Congress enacted the Securities Litigation Uniform
5 Standards Act (“SLUSA”), which empowered federal courts presiding over PSLRA
6 cases to “stay discovery proceedings in any private action in a State court, as necessary
7 in aid of its jurisdiction, or to protect or to effectuate its judgments.” 15 U.S.C. § 78u-
8 4(b)(3)(D). The purpose of the legislation was “to prevent plaintiffs from circumventing
9 the stay of discovery under the [PSLRA] by using State court discovery, which may not
10 be subject to those limitations in an action filed in State court.” H.R. Rep. No. 105-640,
11 at 17-18 (1998) (explaining that the House committee intended courts to use the
12 provision “liberally”) (quoted in In re Dot Hill Sys. Corp. Sec. Litig., 594 F. Supp. 2d
13 1150, 1165 (S.D. Cal. 2008)). Judge Prochnau did not reach the merits of the SLUSA
14 motion.²

15 In determining whether to stay state court discovery, courts generally consider:
16 (1) the risk of federal plaintiffs obtaining the state plaintiff’s discovery, (2) the extent of
17 factual and legal overlap between the state and federal actions, and (3) the burden of
18 state-court discovery on defendants. In re Dot Hill, 594 F. Supp. 2d at 1165. Regarding
19 the first issue, the focus is not whether the state court plaintiffs filed their action to evade
20 the discovery stay. Rather, it “is whether some form of relevant discovery is likely to
21 reach the federal plaintiffs during the pendency of a motion to dismiss in federal court.”
22 In re Cardinal Health, Inc. Sec. Litig., 365 F. Supp. 2d 866, 875 (S.D. Ohio 2005). In this

23
24 ² This Court has the utmost respect for Judge Prochnau having been her colleague on the
25 King County Superior Court. This Court does not take lightly a request to interfere with a state
26 court matter. This is an unusual circumstance where justice requires it.

1 case, the risk is substantial. Plaintiffs do not dispute that much of the discovery they seek
2 will be relevant to a motion to dismiss in this case. Although different counsel represents
3 the state court plaintiffs, the state court plaintiffs are putative members of this federal
4 securities class action. As such, their receipt of discovery “would violate the PLSRA.”³
5 In re Dot Hill, 594 F. Supp. 2d at 1167. Moreover, the state court plaintiffs profess to
6 need the requested discovery to file a motion for injunctive relief, which would be filed
7 and heard publicly. Id. (finding that the risk of disclosure was substantial where
8 “discovery hearings, discovery orders, and perhaps a public trial are likely.”). Although
9 the state court plaintiffs insist that they would agree to a protective order, that promise is
10 not dispositive and would have little effect if information is publicly aired. Id.; see also
11 In re Cardinal Health, 365 F. Supp. 2d at 875-77 (staying discovery “despite the [signed]
12 confidentiality agreement and the good faith efforts of State Plaintiff,” in part because
13 “this Court remains concerned that some form of discovery, whether it be a state court
14 order resolving a discovery dispute or a public hearing, will reach Plaintiffs before this
15 Court has decided any dismissal motion”).

16 Finally, plaintiffs argue that they would be prejudiced by a stay because the delay
17 could result in fading witness memories and similar difficulties. However, the delay is
18 unlikely to be protracted. In addition, “prejudice is not a consideration under the
19 SLUSA.” In re Crompton Corp. Sec. Litig., 2005 U.S. Dist. LEXIS 41031 at * 10 (D.
20 Conn. 2005). Therefore, the first factor weighs in favor of a stay.

21 Plaintiffs contend that the second factor weighs in their favor because their action
22

23 ³ The fact that the state court plaintiffs are also putative plaintiffs in this action means
24 that they are not being forced to “stand aside” while other litigants settle a rule of law that affects
25 their rights, which would militate against a stay. See, e.g., Landis v. North Am. Co., 299 U.S.
26 248, 255 (1936).

1 is derivative rather than a securities class action. However, because the SLUSA dictates
2 that a court may stay discovery “in any private action in a State Court,” “the focus should
3 be on whether discovery in the state action will adversely affect a court’s ability to decide
4 a federal securities action, not whether the state claims mirror the federal claims.” In re
5 Gilead Sciences Sec. Litig., 2004 WL 3712008 at * 4 (N.D. Cal. 2004). The claims in
6 both actions are premised on defendants’ alleged misstatements. The factual allegations
7 in the complaints are substantively identical. Undisputedly, the state court discovery
8 would be useful to the plaintiffs in this action if they were to amend their complaint.⁴
9 Therefore, if state court discovery is permitted, this Court’s jurisdiction to rule on a
10 motion to dismiss the federal claims, before any discovery has been conducted, could be
11 circumvented.

12 Turning to the third factor, the Court evaluates the burden on defendants.
13 Plaintiffs argue that the burden can be minimized through the use of a discovery special
14 master in state court. However, the discovery requests seek extensive discovery, and
15 plaintiffs have not offered any proposal for limiting it. Specifically, the demands
16 comprise 57 document requests, many of which contain sub-parts, and 25 interrogatories
17 on a broad range of topics. Requiring defendants to respond to them would be costly and
18 disruptive to the company’s business operations. That burden is not inevitable because if
19 this Court grants a motion to dismiss, the ruling would likely moot the state court claims.
20 In fact, in the state court action, plaintiffs are seeking to hold the directors and officers
21 liable for any judgment that may be entered against, or costs incurred by, the corporation
22 in this action. Because of the overlapping nature of the claims, absent a stay, defendants

23
24 ⁴ Although plaintiffs suggest that SLUSA’s discovery stay is inapplicable to state
25 derivative actions, courts have held otherwise. See, e.g., In re Dot Hill, 594 F. Supp. 2d at 1166
(citing cases).

1 would be forced to provide discovery related to plaintiffs' claims in this case while the
2 PSLRA stay is in effect. That burden is "extreme[]" and it exists even if the discovery
3 special master ultimately narrows the requests. See, e.g., Buettgen v. Harless, 2010 U.S.
4 Dist. LEXIS 65529 at * 7 (N.D. Tex. 2010); In re Dot Hill, 594 F. Supp. 2d at 1166
5 (explaining that allowing the state court discovery to proceed "would impermissibly
6 burden defendants, who need not participate in discovery regarding securities fraud
7 claims until" after resolution of a motion to dismiss in the federal case); In re Crompton
8 Corp., 2005 U.S. Dist. LEXIS 41031 at *11-12 ("Defendants would be extremely
9 burdened if they had to produce virtually the same discovery [in a state action] that has
10 been stayed pending this Court's resolution of the motion to dismiss this action prior to
11 this Court's decision on that motion."). Therefore, all three factors weigh in favor of
12 granting a stay to protect this Court's jurisdiction to rule on a motion to dismiss prior to
13 discovery.

14 III. CONCLUSION

15 For all of the foregoing reasons, the Court GRANTS defendants' motions to stay
16 discovery in the state court action (Dkt. ## 55, 57) until after this Court has ruled on
17 defendants' anticipated motions to dismiss in this case.

18
19 Dated this 12th day of September, 2011.

20
21 

22 Robert S. Lasnik
23 United States District Judge
24
25